

MEMORANDUM



DATE: May 11, 2011
TO: House Committee on Transportation
FROM: William E. Hamilton
RE: Motor Fuel Taxes, Sales Tax on Motor Fuels, and Tax Collection

This memo provides background information on taxes imposed on motor fuels in Michigan.

The Michigan motorist pays three separate taxes on gasoline purchased at the pump:

Motor Fuel Tax – The state levies a 19-cent per gallon excise tax on gasoline used in motor vehicles. This tax, established in the Motor Fuel Tax Act (2000 PA 403). Revenue from the tax is dedicated by the 1963 Michigan Constitution for transportation purposes. Revenue from the tax is first credited to the Michigan Transportation Fund (MTF) and is then distributed to other funds and programs according to a formula established in Public Act 51 of 1951. The 19-cent per gallon gas tax is expected to generate over \$839 million for transportation in FY 2010-11 and represents approximately 45% of the state funds used to support the state transportation budget.

The state also levies a 15-cent per gallon tax on diesel motor fuel. The tax on diesel motor fuel is established in two acts: the Motor Fuel Tax Act, and the Motor Carrier Fuel Tax Act (1980 PA 119). In-state users of motor fuel are taxed under the Motor Fuel Tax Act; interstate motor carriers are taxed under the Motor Carrier Fuel Tax Act. Together the two diesel fuel taxes are estimated to generate \$122 million in transportation revenue in FY 2010-11.

Federal Excise Tax – In addition to Michigan's 19-cent per gallon gasoline excise tax, the federal government levies an 18.4 cent per gallon federal gasoline excise tax, and a 24.4 cent per gallon diesel fuel excise tax. These taxes are earmarked for the Federal Highway Trust Fund which is distributed to the states for highway and public transportation programs.

Michigan Sales Tax – In addition to the two excise taxes noted above, Michigan levies a 6% sales tax on retail sales, including gasoline purchases. This tax is established in the General Sales Tax Act (1933 PA 167). The sales tax on gasoline sales is based on the motor fuel purchase price, including the federal excise tax, but not including the state motor fuel excise tax.

The Michigan sales tax is subject to earmarking: One hundred percent (100%) of the tax at 2%, and sixty percent (60%) of the tax at 4% is dedicated by the state Constitution to the School Aid Fund. Fifteen percent (15%) of the tax at 4% is constitutionally earmarked for revenue sharing. In addition, a portion of the sales tax on motor fuel and other automotive products is statutorily earmarked, in the Sales Tax Act, to the Comprehensive Transportation Fund for public transportation programs.¹ The balance of sales tax revenue, the amount not otherwise earmarked or appropriated for revenue sharing, is credited to the state General Fund.

How Tax is Collected – Although the retail price paid at the pump includes federal and state excise taxes, as well as the state sales tax, those taxes are not actually collected from the retailer, (i.e. service station). The excise taxes are actually collected by the Michigan Department of Treasury from fuel suppliers as

¹ The Glenn Steil Revenue Sharing Act (1971 PA 140) also earmarks a portion of the sales tax for local revenue sharing. This earmark for "statutory revenue sharing" is subject to appropriation, and the Legislature appropriates less than this statutory earmark.

defined in the Motor Fuel Tax Act. The change in the tax collection point from the retailer to the supplier was effected for the gasoline tax by Public Act 225 of 1992. The change for diesel taxes was made in part by PA 225 of 1992, and completed through Public Act 668 of 2002.

Note that the Motor Fuel Tax Act allows suppliers to deduct 1.5% of the gasoline quantity from taxation to allow for the cost of remitting the tax. This tax expenditure equates to approximately \$13 million. The deduction had been 2% of the gasoline quantity prior to the enactment of Public Act 83 of 1997 (the act that increased the gasoline excise tax from 15 cents per gallon to 19 cents). Prior to 1997 amendment, this deduction had been described in the Motor Fuel Tax Act as an "evaporation and loss allowance."

With regard to the sales tax, the Michigan Department of Treasury sets a prepaid gasoline sales tax rate. This tax is collected from the gasoline refiner or importer at the time fuel is sold to a wholesaler. As a result, the sales tax is included in the price paid by the wholesaler and, in turn, the retail service station. The retailer is credited for the amount of prepaid sales tax at the time he or she prepares a monthly sales tax report. If the retailer had effectively prepaid \$10,000 in sales tax, as included in the price charged by the wholesaler, and the retailer's actual total tax liability for the month was \$11,000, the retailer would remit only the \$1,000 balance to the Department of Treasury. Conversely, if the retailer's actual tax liability were less than the amount of pre-payment, the retailer would be entitled to a credit.

The pre-payment provisions of the Sales Tax Act were amended in 2008 by 2008 PA 556 (Senate Bill 881). Prior to enactment of Senate Bill 881, the Department had been required to determine the prepayment rate every six months, unless the Department certified that the statewide retail price of a gallon of self-serve unleaded regular gasoline had changed less than 10.0% during the six-month period, but not less than annually. Senate Bill 881 required the Department to determine the prepayment rate every three months unless it determined that the statewide average retail price for self-serve unleaded regular gasoline had changed less than 10.0% since the establishment of the rate.

It is our understanding that the change effected by Senate Bill 881, to increase the frequency that the Michigan Department of Treasury adjusted the per-gallon sales tax pre-payment rate for gasoline sales, was intended to help reduce tax overpayments and underpayments